IN THE UNITED STATES BANKRUPTCY COURT

FOR THE

SOUTHERN DISTRICT OF GEORGIA
Savannah Division

IN RE:	)	Chapter 7 Case
	)	Number 87-40943
WILLIAM F. BRAZIEL, JR.	)	
	)	
Debtor	)	
_____)	Filed	
	)	at 4O'clock & 59 min PM
THOMAS L. HENDRIX	)	Date: 5-4-90
	)	
Plaintiff	)	
	)	
vs.	)	Adversary Proceeding
	)	Number 88-4099
WILLIAM F. BRAZIEL, JR.	)	
	)	
Defendant	)	

ORDER

Plaintiff, Thomas L. Hendrix, brought this action objecting to the discharge of a debt in the principal sum of Two Hundred Eighteen Thousand Five Hundred Eighty-Four and 48/100 ($218,584.48) Dollars owed plaintiff by defendant, William F. Braziel, Jr. The court, after considering the pleadings, arguments of counsel, and the evidence presented at trial, makes the following findings of fact and conclusions of law.

FINDINGS OF F~CT

1. Defendant was a practicing attorney in Savannah, Georgia. Defendant and his law firm, Braziel & Braziel enjoyed a substantial real estate practice.

2. Plaintiff owns a substantial amount of real estate valued at between Eight Hundred Thousand and No/100 ($800,000.00) Dollars and One Million and No/100

($1,000,000.00) Dollars.

3. Defendant and his firm worked as attorney for plaintiff in a number of the plaintiff's real estate transactions and other legal matters. During the period of their professional relationship the plaintiff also utilized the services of other attorneys. The plaintiff and defendant were friends. The plaintiff and his now deceased wife were godparents to one of the defendant's children.

4. In late 1986, defendant in his capacity as plaintiff's attorney received an insurance proceeds check in the sum of Eighty-Two Thousand Five Hundred Eighty-Four and 48/100 ($82,584.48) Dollars made payable to plaintiff as the beneficiary on an insurance policy on the life of plaintiff's wife. Plaintiff's wife died in June, 1986. Defendant endorsed the check with the plaintiff's name and deposited the check into the real estate escrow trust account of his law firm.

5. On or about January 9, 1987, defendant approached plaintiff at plaintiff's home and requested a loan in the principal sum of One Hundred Eighty-Six Thousand and No/100 ($186,000.00) Dollars. Defendant informed the plaintiff that he "needed the money real bad," but did not disclose the purpose of the loan. Plaintiff did not request that defendant make such a disclosure.

6. On or about January 14, 1987, defendant borrowed an additional Ten Thousand and No/100 ($10,000.00) Dollars from plaintiff. Again, on or about January 28, 1987, defendant borrowed an additional Fifteen Thousand and No/100 ($15,000.00) Dollars from the plaintiff. At the time of these two loans, the defendant told plaintiff that he needed the loans because he "was in a bind."

7. Promissory notes were executed on each of the three January loans. Plaintiff also testified that a promissory note was executed to cover the life insurance proceeds. No note representing the life insurance proceeds was presented at trial.

8. Plaintiff received interest payments on all sums borrowed by the defendant, including the life insurance proceeds.

9. On April 13, 1987, defendant and his wife executed and delivered to plaintiff a deed to secure debt in the amount of Two Hundred Ninety-Three Thousand Five Hundred Eighty-Four and 48/100 ($293,584.48) Dollars. The deed to secure debt was executed at the request of the plaintiff and included all loans made up to that date, including the proceeds of the insurance check.

10. In July, 1987, the plaintiff loaned the defendant an additional Ten Thousand and No/100 ($10,000.00) Dollars. Also, in July, 1987 the principal sum due plaintiff was reduced by a payment of Seventy-Five Thousand and No/100 ($75,000.00) Dollars from defendant.

11. On October 5, 1987, four (4) of defendant's creditors brought an involuntary Chapter 7 petition against the defendant after learning that the defendant had failed to utilize loan proceeds turned over to the defendant at various real estate closings to pay off prior loans on the real property that was the subject of the closings.

12. Defendant has voluntarily surrendered his license to practice law and stands disbarred. In January, 1989, the defendant pleaded guilty to seven (7) counts of theft of clients' funds and was sentenced to serve a ten (10) year prison term.

13. Funds obtained from plaintiff were used by defendant to cover shortages in the trust account of defendant's law firm.

14. The testimony of the plaintiff and defendant relative to the $82,584.48 insurance proceeds check differs substantially. According to the defendant, he first approached the plaintiff for a loan of $40,000.00 in October, 1986. In response to the solicitation, the plaintiff advised the defendant that if he would do his job and get the insurance claim settled, the plaintiff would loan the defendant the entire insurance proceeds. The proceeds were received by the defendant acting as plaintiff's attorney and deposited into the defendant's real estate escrow trust account by the defendant signing the plaintiff's name as endorsement to the check. According to defendant this deposit practice had been followed by the defendant in

representing the plaintiff without objection. According to defendant, plaintiff knew of the insurance proceeds deposit and approved the loan of the funds to defendant. Defendant contends that a note was drawn in December, 1986, to evidence the loan of the entire insurance proceeds and presented to the plaintiff. According to the defendant the plaintiff requested modification in the note term which was agreed to by the defendant. Neither an original, nor a revised note, in the amount of Eighty Two Thousand Five Hundred Eighty-Four and 48/100 ($82,584.48) Dollars was submitted as evidence in this proceeding. Plaintiff contends that he did not know that the insurance proceeds had been received by the defendant until February, 1988 when plaintiff received a tax statement from the insurance company issuing the check. Several facts rebut plaintiff's contention. First, the plaintiff admits that he received monthly interest payments on the entire insurance proceeds as early as March, 1987. Secondly, the deed to secure debt dated April 13, 1987, indicates a loan amount which includes the insurance proceeds. Finally, the plaintiff admitted that he extended an additional Ten Thousand and No/100 ($10,000.00) Dollars to the defendant in July, 1987 after he had learned of the defendant's conduct relative to the insurance proceeds. Assuming that the plaintiff is mistaken as to the year

and that he first learned of the insurance proceeds check in February, 1987, the plaintiff's conduct relative to the defendant after this date is more indicative of a borrower and lender relationship than that of a thief and victim. The plaintiff admitted receiving monthly interest payments on the insurance proceeds. The personal and professional relationship of the plaintiff and defendant continued until at least July, 1987. The plaintiff extended an additional loan of Ten Thousand and No/100 ($10,000.00) Dollars in July 1987 after he admittedly knew of the insurance proceeds. From the evidence, as it pertains to the insurance proceeds in the amount of Eighty-Two Thousand Five Hundred Eighty-Four and 48/100 ($82,584.48) Dollars, I find the defendant's testimony to be credible. The insurance proceeds were lent by the plaintiff to the defendant in the same manner as the other loan transactions between the parties.

CONCLUSIONS OF LAW

In his complaint, plaintiff proceeds under 11 U.S.C. §523(a)(4)[1] and contends that the obligations owed plaintiff by

defendant should be nondischargeable debts because the debts were incurred by fraud, or defalcation while acting in a fiduciary capacity, embezzlement, or larceny. At the trial of this case, it became apparent that the plaintiff intended also to proceed under 11 U.S.C. §523(a)(2)(A)[2] by contending that the defendant's debt to the plaintiff was incurred as a result of false pretenses, false representations, or actual fraud. The defendant made no objection to proceeding under this provision. In accordance with Bankruptcy Rule 7015, the pleadings are amended to conform to the evidence presented at trial to include allegations under both sections 523(a)(4) and 523(a)(2)(A). See Fed. R. Civ. P. 15(b).

"Because of the very nature and philosophy of the bankruptcy law the exceptions to dischargeability are to be construed strictly, Gleason v. Thaw, 236 U.S. 558, 35 S.Ct. 287, 55 L.Ed. 717 (1915), and the burden is on the

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[1]11 U.S.C. §523(a)(4) provides in relevant part:

> (a) A discharge under section 727 . . . of this title does not discharge an individual debtor from any debt
>
> (4) for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny.

[2]11 U.S.C. §523(a)(2)(A) provides in relevant part:

> (a) A discharge under section 727 . . . of this title does not discharge an individual debtor from any debt
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> (2) for money, property, services, or an extension, renewal, or financing of credit, to the extent obtained by
>
> (A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition.

creditor to prove the exception. Danns v. Household Finance Corp., 558 F.2d 114 (2nd Cir.

1977)." Schweig v. Hunter (In re: Hunter), 780 F 2d 1577, 1579 (11th Cir. 1986). The creditor must prove the debtor's culpability by clear and convincing evidence. Id. In this case plaintiff, has failed to meet that burden of proof to have the obligations owed him by the defendant held to be an exception to discharge.

"In order to preclude the discharge of a particular debt because of a debtor's false representation, a creditor must prove that: the debtor made a false representation with the purpose and intention of deceiving the creditor; the creditor relied on such representation; his reliance was reasonably founded; and the creditor sustained a loss as a result of the presentation." Schweig, supra at 1579. The plaintiff contends that the defendant's failure to reveal the actual purpose for which he needed the funds amounts to obtaining the loans though false pretenses, a false representation, or actual fraud. The basis of plaintiff's contention is that the defendant had a duty to voluntarily reveal the problems with the trust account of his law firm and his financial instability. Binding precedent in this circuit is to the contrary. As the Eleventh Circuit Court of Appeals has noted, the "[b]ankruptcy law does not mandate that a debtor voluntarily disclose without solicitation by a creditor, his personal habits, tendencies, welfare, and lifestyle, such as marital and family related problems, alcoholism, compulsive gambling, and current state of physical and mental health, all of which may affect, directly or

indirectly, the debtor's ability to satisfy his debts and obligations . . . ." Schweig, supra at 1580. "[T]here must be actual overt false pretense or representation to come within the exception." Id. See also Davison-Paxon Co. v. Caldwell, 115 F.2d 189 (5th Cir. 1941), cert. denied, 313 U S. 564, 61 S.Ct. 841, 85

L.Ed. 1523 (1941).[3] The failure of the defendant to voluntarily reveal or confess his trust account transgressions to the plaintiff is not sufficient to preclude the discharge of the debt under section 523(a)(2)(A).

The plaintiff also contends that the defendant told him he was receiving a second in priority lien on all of the property included in the deed to secure debt executed by the defendant and his wife and delivered to plaintiff. Defendant contends that plaintiff knew of the outstanding second security deeds ahead of plaintiff's security interest. Even assuming that the plaintiff is correct, the plaintiff admits that he never checked the titles to the properties despite his knowledge of real estate and the need for a title search. Instead, plaintiff chose to rely on the alleged oral statements of the defendant as to the status of his liens on

the properties. In support of his contention that the reliance on the oral statements of the defendant was reasonable, the plaintiff erroneously relies on the decision of the Sixth Circuit Court of Appeals in the case of Coman v. Phillips (In re: Phillips), 804 F.2d 930 (2nd-Cir. 1986). In Phillips, the court concluded that the reliance of the plaintiff on the statements of the defendant as to the amount of property the defendant owned was reasonable given the twenty-five (25) year personal relationship between the plaintiff and the defendant, and the presentation of the original deed to the property to the plaintiff without reference to the fact that much of the property had been conveyed to others in prior transactions. The plaintiff in this case now before the court, Hendrix, and the defendant, Braziel,

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[3]The Eleventh Circuit Court of Appeals adopted all decisions rendered by the Fifth Circuit Court of Appeals on or before September 30, 1981 as binding precedent in this circuit. Bonner v. City of Prichard, 661 F.2d 1206 (11th Cir. 1981). The Eleventh Circuit specifically reaffirmed that Davison-Paxon Co. remains the law of this circuit in Schweig.

were personal friends, and the defendant represented the plaintiff in numerous real estate closings. The plaintiff contends that this personal relationship is sufficient to warrant the plaintiff's failure to check the titles on the property and to rely on the defendant's alleged statements as to the priority of his liens on the property.

This circuit court, however, has been less willing to remove the duty to make a reasonable inquiry into a debtor's creditworthiness from the shoulders of a prospective creditor. See, Schweig, supra. In Schweig, the debtor/defendant Hunter, a stockbroker who managed the account of Schweig, persuaded Schweig to loan him One Hundred Sixty-Eight Thousand and No/100 ($168,000.00) Dollars. "Schweig never questioned Hunter about his financial condition - - personal or otherwise. Schweig also did not ask for a financial statement or run a credit check before making the loan. Hunter ultimately defaulted on the note after partially repaying it . . . ." Schweig, supra at 1578. In Schweig, the court found that the facts established "an example of misplaced trust and a failure to investigate creditworthiness or to ferret out ordinary credit information." Schweig, supra at 1580. The court concluded that "the failure to use ordinary precautionary measures prior to making a sizable loan" did not warrant a finding that the debt should be precluded from discharge in the broker's Chapter 7 bankruptcy proceeding. Id.

Schweig is too close in both facts and issues to this case to be ignored. The plaintiff, an experienced real estate investor, mistakenly relied on an alleged oral representation by the defendant rather than following the prudent course of investigating the titles to property which would have revealed the prior liens. The defendant provided no written financial data to the plaintiff, and the plaintiff asked no questions before making sizable loans to the defendant. Plaintiff failed to take ordinary precautions, and that failure should not bar the discharge of the defendant's debt to the plaintiff.

Plaintiff also argues that the obligations owed him by the defendant should be precluded from discharge based upon the

defendant's fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny. 11 U.S.C. §523(a)(4). The only funds obtained by defendant while acting in a fiduciary capacity for the plaintiff was the check for the life insurance proceeds in the sum of Eighty-Two Thousand Five Hundred Eighty-Four and 48/100 ($82,584.48) Dollars received by the defendant while acting in his capacity as the plaintiff's lawyer. Having found that the parties intended the insurance proceeds to be utilized as a personal loan by the defendant, when the defendant applied the insurance proceeds to his own use, he was not acting as a fiduciary, but as a borrower. The defendant committed no fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny. He borrowed the money and failed to repay it. No reason exists to preclude these obligations from the discharge allowed by 11 U.S.C. §727.

The court is aware of the harsh result of this decision on the plaintiff, but as the Eleventh Circuit Court of Appeals has noted, misplaced trust and the failure to use ordinary precautionary measures prior to loaning an individual substantial amounts of money is insufficient to bar the discharge of the obligation in bankruptcy. The defendant has admitted committing grievous acts concerning clients' funds. The defendant broke the law, disgraced himself and his family, and is paying an appropriate price. However, he has not committed any act with regard to the loans obtained from plaintiff which would bar the discharge of those obligations. The funds received were personal loans that the defendant failed to repay - - nothing more.

It is therefore ORDERED that judgment is hereby entered in this adversary proceeding in favor of defendant, William F. Braziel, Jr., and against plaintiff, Thomas L. Hendrix. The defendant is not entitled to any monetary recovery under 11 U.S.C. §523(d) as the plaintiff's position was not so substantially unjustified as to warrant any recovery to the defendant. No monetary award shall be entered.

JOHN S. DALIS

UNITED STATES BANKRUPTCY JUDGE

Dated at Augusta, Georgia

this 4th day of May, 1990.